

D.T.E. 01-73

Petition of Colonial Gas Company for the recovery of lost-based revenue associated with its demand-side management programs for the period May 2000 through April 2001

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FOR: Colonial Gas Company d/b/a/ KeySpan Energy Delivery
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I. INTRODUCTION

On September 17, 2001, Colonial Gas Company, doing business as KeySpan Energy Delivery New England (“Colonial” or “Company”), filed two petitions with the Department. The first petition sought the Department’s approval concerning the Company’s recovery of lost-based revenue (“LBR”) of \$288,822 that the Company incurred from May 2000 through April 2001 for demand-side management (“DSM”) programs. The Company filed this petition in accordance with the rolling-period methodology the Department adopted in Colonial Gas Company, D.T.E. 97-112 (1999) (“D.T.E. 97-112”). The second petition sought LBR recovery of \$1,034,093 for the same period of May 2000 through April 2001. The Company seeks to recover LBR as an exogenous cost adjustment in accordance with the ten-year rate plan approved by the Department in Eastern-Colonial Acquisition, D.T.E. 98-128 (1999) (“Merger Order”). The Department considered both petitions and combined them under docket number D.T.E. 01-73.

The Department combined the two petitions into one docket to be consistent with Department precedent. In Colonial Gas Company, D.T.E. 00-73, the Department also combined the Company’s two petitions into one filing. Because the Department issued that order after the Company filed the instant petitions, Colonial filed a supplemental filing with the Department on January 24, 2002 to address the Department’s directives in D.T.E. 00-73.

The Department held a public hearing on January 16, 2002. There were no intervenors in this matter. The Department held an evidentiary hearing on March 20, 2002. The evidentiary record consists of the two Company’s filings, its supplemental filing, and all of the responses to the Department’s information and record requests. On April 9, 2002, the

Company filed a brief on the issues presented at the evidentiary hearing.

II. LBR RECOVERY FOR DSM MEASURES

A. Standard of Review

In evaluating savings estimates for gas DSM programs, the Department will draw on its experience with electric DSM programs. Bay State Gas Company, D.P.U. 96-98, at 1 (1997). The Department has found that many estimates of savings that are not actually measured have been biased upward substantially, and has therefore required companies to measure savings using impact evaluations. Massachusetts Electric Company, D.P.U. 92-217-B, at 4-5 (1994) (“MECo”). The Department has identified and approved a wide variety of techniques for evaluating savings estimates. See id. at 7-16, 35-38, 47-51, 68-74. However, the Department has found many cases where appropriate techniques have not been applied or have been misapplied to produce savings estimates that are biased upward or downward. See id. at 5; Boston Edison Company, D.P.U. 96-1-CC, at 3-4, 9-12, 21-22, 24 (1996). Recognizing that obtaining more precise savings estimates has a cost, the Department directed companies to seek increased precision to the extent that the marginal value of more precise estimates exceeds the marginal cost of obtaining the additional precision. MECo at 5.

In MECo, the Department introduced a standard of review to be applied to impact evaluations.¹ The Department has used the same standard for gas DSM evaluations: in order for a company’s DSM savings estimates to be accepted, the company must demonstrate that its impact evaluations are reviewable, appropriate, and reliable. D.P.U. 96-98, at 2, citing MECo

¹ Impact evaluations use quantitative analyses to assess energy and capacity savings resulting from the implementation of DSM programs. MECo at 1.

at 4-6. An impact evaluation is considered reviewable if it is complete, clearly presented, and contains a summary that sufficiently explains all assumptions and data presented. MECo at 4-6. An impact evaluation is considered appropriate if evaluation techniques selected are reasonable given the characteristics of a particular DSM program, the company's resources, and the available methods for determining demand and energy savings estimates. Id. Finally, an impact evaluation is considered reliable if the savings estimates included in the evaluation are unbiased and are measured to a sufficient level of precision, given the characteristics of a particular DSM program, the company's resources, and the available methods for determining demand and energy savings estimates. Id.

In Boston Gas Company, D.P.U. 94-15 (1995) ("D.P.U. 94-15"), the Department ordered local distribution companies ("LDCs"), when petitioning for the recovery of LBR and incentives from DSM programs, to develop energy savings estimates for their residential and multifamily programs using the Gas Evaluation and Monitoring Study ("GEMS")² method,³ subject to certain conditions. See D.P.U. 94-15, at 52-54.

² GEMS was a comprehensive research project which used a variety of analytical tools to evaluate the effectiveness of residential and multi-family natural gas DSM programs. D.P.U. 94-15, at 1 n.1.

³ GEMS method refers to the overall analytical framework established by Boston Gas Company to: (1) determine the effectiveness of Boston Gas Company's residential DSM programs by estimating the amount of gross energy saved from a sample of its residential customers; (2) transfer these results to its residential DSM and non-host local distribution companies' DSM programs; and (3) adjust gross savings to account for factors that affect net program savings. Id., at 1 n.2.

B. The Company's DSM Impact Evaluations

1. Overview

In this proceeding, the Company submitted two LBR recovery filings for its Residential and Commercial & Industrial ("C&I") DSM Programs. For the first filing ("standard filing"), the Company calculated the LBR and associated carrying costs using the rolling-period methodology approved by the Department in D.T.E. 97-112. DSM measures installed by the Company before May 1, 1997, were not included in estimating total energy savings in the standard filing (Exh. KSE-1, at 1). For the second filing ("exogenous cost filing"), Colonial calculated the total energy savings, the LBR, and associated carrying costs, based on the methodology approved by the Department prior to D.T.E. 97-112, and included all DSM measures installed by the Company between October 1992 and April 2001, with the exception of the measures already included in the standard filing (Exh. KSE-2).

Colonial requests the recovery of LBR and carrying costs associated with its Residential and C&I DSM programs of \$1,322,914.54 for the period May 2000 through April 2001 (Exh. KSE-1, Attachment A). Colonial proposes to recover \$288,821.53 pursuant to the rolling-period method approved by the Department in D.T.E. 97-112 and the remaining \$1,034,093.01 as an exogenous cost pursuant to the ten-year rate plan approved in the Merger Order (*id.*). The Company proposes to recover each amount over a twelve-month period, starting from November 1, 2001 (Exh. KSE-1, at 1; Exh. KSE-2, at 1).⁴ The following sections break down this total amount by customer class.

⁴ The Department notes that the Company's local distribution adjustment factor ("LDAF") approved on October 31, 2001 includes all of the LBR and carrying costs proposed for recovery in this proceeding.

2. Residential Programs

a. Description

In the standard filing, the Company calculated the LBR and associated carrying costs using the rolling-period methodology approved by the Department in D.T.E. 97-112 (Exh. KSE-1). The Company did not include DSM measures that it installed before May 1, 1997 in estimating total energy savings in the standard filing. In the exogenous cost filing, Colonial calculated the total energy savings, the LBR, and associated carrying costs, based on the methodology prior to D.T.E. 97-112, and included all DSM measures installed by the Company before and after May 1, 1997 except the measures already included in the standard filing (Exh. KSE-2).

Colonial stated that it used the GEMS method, approved in D.P.U. 94-15, to calculate the savings per thousand cubic feet ("Mcf") for its residential DSM programs under both the standard filing and the exogenous cost filing (Exh. KSE-1, exh. 1, at 1). In the standard filing, Colonial estimated net energy savings for its residential DSM program of 31,451.89 Mcf for the period May 2000 through April 2001 (Exh. KSE-1, exh. 3). Based upon these estimates, the Company requests the recovery of \$103,573.61 in LBR associated with its residential DSM program, plus carrying costs of \$26,504.17, totaling \$130,077.78 for the period May 2000 through April 2001 (Exh. KSE-1, exh. 3). In the exogenous cost filing, the Company estimated a net energy savings amount for its residential DSM program of 196,745.91 Mcf for the period May 2000 through April 2001 (Exh. KSE-1, Attachment A). Based upon these estimates, the Company requests the recovery of \$638,908.15 in LBR associated with its Residential program, plus carrying costs of \$68,908.10 or \$707,816.25 in total (Exh. KSE-1,

Attachment A).

b. Analysis and Findings

The Department has reviewed the Company's estimates of savings associated with its residential DSM programs. The Department notes that Colonial's method of calculating the residential program savings is the same as the method approved by the Department in Colonial Gas Company, D.T.E. 00-73 (2001); Colonial Gas Company, D.T.E. 98-95/99-82 (2000) and D.T.E. 97-112. The Department finds that the Company appropriately applied the GEMS Method to calculate its energy savings estimates. Accordingly, the Department finds both the Company's estimates of energy savings and the method for calculating exogenous costs for its residential program to be reliable, reviewable, and appropriate, and hereby accepts them. Therefore, the Department approves the recovery of LBR associated with the Company's residential DSM program of \$103,573.61 plus carrying costs of \$26,504.17 totaling \$130,077.78 for the period May 2000 through April 2001. The Department will address the Company's request to recover LBR and associated carrying costs as an exogenous cost pursuant to the Merger Order in Section III, below.

3. C&I Programs

a. Description

As was the case with respect to its residential DSM programs, the Company submitted two LBR recovery filings for its C&I DSM Programs. In the standard filing, the Company calculated the LBR and associated carrying costs using the four-year rolling-period methodology approved by the Department in D.T.E. 97-112 (Exh. KSE-1). The Company did not include DSM measures it installed before May 1, 1997 in estimating total energy savings in

the standard filing. In the exogenous cost filing, Colonial calculated the total energy savings, the LBR, and associated carrying costs, based on the methodology used by the Department prior to D.T.E. 97-112, and included all DSM measures installed by the Company before and after May 1, 1997, except the measures already included in the standard filing (Exh. KSE-2).

In both filings, the Company stated that it used the impact evaluation process, the Mcf savings calculations, and lost margin and financial incentive calculations approved by the Department in Colonial Gas Company, D.P.U. 96-31 (1996) to calculate Mcf savings and lost margins for its Small and Medium C&I DSM programs (Exh. KSE-1, exh. 4, at 1). In the standard filing, Colonial estimated a net energy savings for its Small C&I program of 7,965.20 Mcf, and a gross energy savings amount for its Medium C&I program of 41,131.01 Mcf for the period May 2000 through April 2001 (Exh. KSE-1, exhs. 6, 8). Based upon these estimates, the Company requests the recovery of \$131,355 in LBR associated with its C&I DSM program, plus carrying costs of \$27,389, totaling \$158,744 for the period May 2000 through April 2001 (Exh. KSE-1, exh. 4, at 1). In the exogenous cost filing, the Company estimated a net energy savings amount for its Small C&I program of 33,781.1 Mcf, and a gross energy savings amount for its Medium C&I program of 78,692.34 Mcf, for the period May 2000 through April 2001 (Exh. KSE-2, exhs. 6, 8). Based upon these estimates, the Company requests the recovery of \$300,169.49 in LBR associated with its C&I DSM program, plus carrying costs of \$26,107.27, or \$326,276.76 in total (Exh. KSE-2, exh. 4, at 1).

The Company proposed to recover the LBR and associated carrying costs over a twelve-month period beginning November 1, 2001. As described below, Colonial used different methods to calculate energy savings for its Small and Medium C&I Programs.

b. Savings Estimates

i. Small C&I Program

Colonial's Small C&I Program consists of three steps: (1) energy assessment; (2) installation of selected measures; and (3) quality control inspection (Exh. KSE-1, exh. 4, at 2; Exh. KSE-2, exh. 4, at 2). The Company offered 13 gas savings measures to eligible customers (Exh. KSE-1, exh. 4, at 2; Exh. KSE-2, exh. 4, at 2). These customers included Small C&I customers on rate classes G-41 and G-51 (id.). Customers who participated in the program received a full (100 percent) subsidy for installations of recommended measures (id.).

The Company indicated that in order to calculate net Mcf savings for each measure, it discounted the annualized gross savings figure for each measure by a free rider estimate and persistence factor (Exh. KSE-1, exh. 4, at 3). The Company defined a free rider as a customer who planned to install a measure on his own (the same amount or more, sooner or at the same time) prior to program participation (id.). Colonial stated that a persistence factor accounts for measures that are still installed and operating properly (id.). The Company explained that it developed these free rider estimates and persistence factors in D.P.U. 96-31 as part of the impact evaluation analysis (id.).

The Company's impact evaluation study indicated that the overall realization rate for Small C&I Program is 107 percent, with a realization rate of 115 percent in the Lowell Division and 75 percent in the Cape Cod Division (Exh. KSE-1, exh. 4, at 2).⁵ Colonial

⁵ A DSM tracking system contains estimates of the savings based on the original engineering estimate of savings for each measure. D.P.U. 96-98, at 4. An impact evaluation, on the other hand, estimates the amount of savings actually achieved. Id. The ratio of this latter estimate to the former tracking estimate is called a "realization rate." Id.

explained that gross savings estimated through the impact evaluation were 107 percent of the savings expected using the Company's engineering data for this program (id.). The Company further explained that, to calculate total program energy savings, it multiplied engineering savings estimates, or in this case technical potential savings estimates, for the entire population of program participants by the realization rate (id.).

Based on the four-year rolling-period method, the Company's total net Mcf savings attributable to the Small C&I Program for May 2000 through April 2001 amounted to 7,965.20 Mcf (6,760.33 Mcf in the Lowell Division and 1,204.87 Mcf in the Cape Cod Division) (Exh. KSE-1, exh. 6). Using the old methodology with which the Department calculated energy savings for all DSM measures installed before and after May 1, 1997, the Company's total net Mcf savings attributable to the Small C&I Program for the period May 2000 through April 2001 amounted to 41,749.71 Mcf (35,809.89 Mcf in the Lowell Division and 5,939.41 Mcf in the Cape Cod Division) (Exh. KSE-3, exh. Supp-3). The Company used the total net monthly Mcf savings to calculate the LBR and associated carrying costs for its Small C&I Program for the Lowell and Cape Cod Divisions in both filings (Exh. KSE-1, exhs. 5, 6, 9).

ii. Medium C&I Program

The Company stated that customers on rate classes G-42 and G-52 were eligible for its Medium C&I Program (Exh. KSE-1, exh. 4, at 3). The Medium C&I Program involved five steps: (1) energy audit; (2) evaluation of cost effectiveness measures and presentation of analysis; (3) contractor quotes and selection; (4) installation of selected measures; and (5) quality control inspection. The Company offered 27 gas savings measures through the Medium C&I Program (id.).

The method of calculating energy savings for the Medium C&I Program in the standard and exogenous cost filings was different from the engineering savings estimates method used for the Company's Small C&I Program. In calculating gross energy savings for its Medium C&I Program, the Company stated that it derived initial savings estimates by using customer-specific facility audit data (Exh. KSE-1, exh. 4, at 4). The Company stated that it used "Market Manager," an energy audit and modeling software package developed by Synergic Resource Corporation, to identify appropriate gas savings measures, and the associated cost and estimated savings for each customer (Exh. KSE-1, exh. 4, at 4). The Company further explained that for each customer, Market Manager created an energy model that simulated the energy use of a facility prior to the installation of any measure (id.). The Company then added savings measures to the model to obtain gross estimated annualized Mcf savings for each program participant customer (Exh. KSE-1, exh. 4, at 4; Exh. KSE-3, at 5-6). In response to a Department directive in D.T.E. 00-73 to address the merits of calculating gross versus net savings for the medium C&I program, Colonial explained that, in November 1995, prior to the Company's filing in Colonial Gas Company, D.P.U. 96-31, the Company asked Tellus Institute ("Tellus") to perform an impact evaluation of its C&I DSM programs so that it could use the results to update the Market Manager model for each customer with more accurate customer-specific information gathered subsequent to program participation (Exh. KSE-3, at 6). The Company stated that the results of the Tellus study showed that the actual gross Mcf savings from the medium C&I program were 113 percent of the gross Mcf savings estimates calculated using Market Manager (id.). The Company explained that Tellus indicated that they were unable to provide reliable information on two of the behavioral factors, free riders and

persistence, which are generally used to adjust gross Mcf savings to net Mcf savings (id.). The Company stated that, based on the recommendation of the Tellus study, it did not increase the Market Manager Mcf savings estimates to reflect the study's projected realization rate, but simply used the initial Market Manager Mcf savings estimates to calculate a conservative savings estimate of its medium C&I program (id.). The Company stated that it used the same methodology to calculate Mcf savings estimates for its medium C&I program in Colonial Gas Company, D.P.U. 96-31 and Colonial Gas Company D.T.E. 00-73 (Exh KSE-3, at 7; Company Brief at 10).

Colonial stated that in order to make any downward adjustment from gross Mcf savings estimate to net Mcf savings estimate, the Company would first have to adjust the Market Manager savings estimates by 13 percent to reflect the results of the Tellus evaluation study (id.). The Company explained that based on a review of the percentage difference between gross and net Mcf savings estimates for its small C&I DSM program, it believes that the 13 percent upward adjustment to the Market Manager savings estimates to reflect the results of the Tellus study would more than off-set any downward adjustment to these estimates to account for free ridership and persistence (id.).⁶

The Company stated that it would need to conduct a detailed survey of program

⁶ The Company stated that a review of the Mcf savings estimates from its small C&I program showed that, on average across all DSM measures, net Mcf savings are 90.46 percent of gross Mcf savings. The Company explained that if it were to adjust upward its medium C&I savings estimates to reflect the results of the Tellus study and then apply the average difference between net and gross savings seen in the small C&I program, the net result would be an increase of approximately \$9,200 in the total LBR and exogenous cost adjustment sought by the Company in this proceeding (Exh. KSE-3, at 7, n.5).

participants to collect the necessary information to estimate free ridership and persistence factor (Exh. KSE-3, at 6-7). The Company explained that given that Colonial has largely moved away from offering traditional retrofit-type DSM programs to participating in collaborative market transformation initiatives, and given that conducting such a survey would be time-consuming and costly for ratepayers, it believes that the methodology used in calculating Mcf savings estimates for its medium C&I program is reasonable, and that no further adjustment is warranted (Exh. KSE-3 at 7; Company Brief at 10-11).

The Company's filing showed that, based on the four-year rolling-period methodology, Colonial's total gross Mcf savings attributable to the Medium C&I Program for the period May 2000 through April 2001 amounted to 41,129.11 Mcf (32,702.71 Mcf in the Lowell Division and 8,426.40 Mcf in the Cape Cod Division) (Exh. KSE-1, exh. 8). Based on the methodology prior to D.T.E. 97-112 ("the old methodology") which calculated energy savings for all DSM measures installed before and after May 1, 1997, the Company's total gross Mcf savings attributable to the Medium C&I Program for the period May 2000 through April 2001 amounted to 119,823.35 Mcf (84,757.05 Mcf in the Lowell Division and 35,066.30 Mcf in the Cape Cod Division) (Exh. KSE-2, exh. 8). The Company used these savings estimates as input into the calculation of Colonial's LBR and associated carrying costs for the Medium C&I Program for the period May 2000 through April 2001 for both filings (Exh. KSE-1, exh. 9; Exh. KSE-2, exh. 9).

c. Analysis and Findings

The Department notes that, in this proceeding and for both filings, Colonial used the same evaluation methods previously approved in D.P.U. 96-31, D.T.E. 97-112 and more

recently D.T.E. 00-73 to determine total energy savings for its Small and Medium C&I DSM programs. In accordance with D.T.E. 97-112, the Company's LBR calculations based on the four-year rolling-period method did not include energy savings associated with DSM measures installed before May 1, 1997. The LBR calculation in the exogenous cost filing, however, included DSM measures installed before and after May 1, 1997. The Department's review of the record shows that the Company's impact evaluations for both the Small and Medium C&I Programs were complete and clearly presented, with all data and assumptions sufficiently explained. Accordingly, the Department finds that the Company's impact evaluations for its C&I DSM programs are reviewable. Furthermore, upon review of the record in this case, the Department finds that the evaluation techniques that Colonial used for its C&I programs are reasonable and are consistent with previous Department Orders. Therefore, we find that the Company's impact evaluations for its C&I programs are appropriate.

The Department accepts the Company's explanation regarding the methodology used to calculate Mcf savings estimates for Colonial's medium C&I program. The Department notes that the methodology used in this case strikes a reasonable balance between the costs that the Company would incur to collect the additional information in order to adjust the gross Mcf savings estimates to net Mcf savings estimates and the gain in precision from such an undertaking.

On the whole, the Department finds that the Company's energy savings estimates for its C&I programs are reliable and were calculated in accordance with the methodology approved by the Department in D.P.U. 96-31. The Company's LBR in the standard filing was also calculated using the four-year rolling-period method approved by the Department in D.T.E. 97-

112, at 33, D.T.E. 98-95/99-82, and D.T.E. 00-73. Therefore, the Department approves the recovery of LBR associated with the Company's C&I DSM program of \$131,355, plus carrying costs of \$27,389, or \$158,744 in total, for the period May 2000 through April 2001. The Department will address the Company's request to recover LBR and associated carrying costs as an exogenous cost pursuant to the Merger Order, in Section III, below.

III. LBR RECOVERY THROUGH EXOGENOUS COST ADJUSTMENT

A. Company Proposal

In addition to the \$288,822 LBR the Company seeks to recover under the rolling-period methodology, Colonial also seeks the recovery of \$1,034,093 in LBR through its Local Distribution Adjustment Clause ("LDAC") as an exogenous cost pursuant to the Merger Order. The \$1,034,093 is comprised of \$707,816 in LBR associated with its residential DSM program, and \$326,277 in LBR associated with its C&I DSM program (Exh. D.T.E. 1-14).

The Company contends that the Department should grant LBR recovery of \$1,034,093 because such recovery satisfies the Department's standard for the recovery of exogenous costs in accordance with the Merger Order (Exh. KSE-2). Colonial notes that in the Merger Order, the Department found that a change in the Department's regulatory policy, including LBR policy, that had cost consequences, could be encompassed under the definition of an exogenous cost, and then established an exogenous cost qualifying threshold of \$250,000 for Colonial based on the relative magnitude of the Company's 1998 operating revenues (id. at 11-12). The Company argues, therefore, that it has satisfied the "Department's two-pronged standard" because: (1) the Company has incurred a cost consequence as a direct result of the Department's policy change in DSM calculation in D.T.E. 97-112 and (2) the exogenous cost

of \$1,034,093 is greater than the established threshold to qualify for recovery (id. at 12).

The Company further contends that Colonial's 2001 return on equity ("ROE") of 3.21 percent is significantly lower than the ROE allowed by the Department for LDCs in recently litigated cases (RR D.T.E-2.).⁷ Colonial notes that a rejection of the Company's proposal to recover the sum of \$1,034,093 as exogenous costs would further reduce the Company's earned ROE for 2001 (id. at 13).

B. Standard of Review

The Department will evaluate the Company's ability to recover LBR through an exogenous cost adjustment in part based on its determinations concerning the requirements for exogenous cost recovery in previous Orders. Merger Order, D.T.E. 98-128 (1999);

NIPSCO-Bay State Acquisition, D.T.E. 98-31 (1998); Eastern-Essex Acquisition, D.T.E. 98-27 (1998); Boston Gas Company, D.P.U. 96-50 (Phase I) (1996).

The Department has defined exogenous costs as positive or negative cost changes beyond a company's control that would significantly affect the company's operations. Merger Order at 54; NIPSCO-Bay State Acquisition at 17, Eastern-Essex Acquisition at 19. Included in that definition are cost changes resulting from: changes in tax laws that uniquely affect the local gas distribution industry; accounting changes unique to the local gas distribution industry; and regulatory, judicial or legislative changes uniquely affecting the local gas distribution industry. Boston Gas Company, D.P.U.96-50 (Phase I) at 292; NIPSCO-Bay State Acquisition at 17, Eastern-Essex Acquisition at 19. In the Merger Order at 55, the Department accepted

⁷ Colonial notes that the Department recently approved an ROE for Berkshire Gas Company of 10.5 percent in Berkshire Gas Company, D.T.E. 01-56 (2002).

the Company's proposal that for Colonial, a change in our regulatory policy regarding LBR, that had cost consequences, be deemed an exogenous cost eligible for proposed recovery.

Further, to avoid costly regulatory process over minimal dollars, the Department has stated that cost changes must meet a monetary threshold, based on a company's size, for qualification to be proposed as an exogenous cost. Merger Order at 55; NIPSCO-Bay State Acquisition at 18; Boston Gas Company, D.P.U. 96-50 (Phase I) at 293. The Department established thresholds on a company-specific basis to reflect a "principle of proportionality" in relation to the company's operating revenues. Merger Order at 55-56. The Department determined that any individual exogenous cost must exceed the Company's threshold in a particular year in order for the Petitioners to request recovery of that particular exogenous cost increase. Id. at 55-56; NIPSCO-Bay State Acquisition at 18; D.P.U. 96-50 (Phase I) at 293. In Colonial's case, the Department established a monetary threshold of \$250,000. Merger Order at 56. To recover exogenous costs during a rate plan, Petitioners are required to propose exogenous cost adjustments, with supporting documentation and rationale, to the Department for determination as to the appropriateness of recovery of the proposed exogenous costs. Id. at 55; NIPSCO-Bay State Acquisition at 17-18.

The Department also has indicated that for rate plans approved pursuant to the merger filings that are not performance base regulation ("PBR") plans, there will be no change to the traditional cost of service regulation by which the Department currently regulates the rates of the companies. Merger Order at 16. Accordingly, during the duration of each rate plan, the earnings of the companies will be a factor in consideration of whether the Department will approve a request for recovery of an exogenous cost. Based on the foregoing, proponents of

an exogenous cost adjustment bear the burden of demonstrating: (1) that the cost change is of a type that is external to the company and is “beyond the company’s control”; (2) that the magnitude of the cost change is such so as to significantly affect the company’s operations; and (3) that the company’s earnings, independent of recovering a proposed exogenous cost, are reasonable.

C. Analysis and Findings

As stated above, the Company seeks to recover \$1,034,093 of LBR as an exogenous cost adjustment. This amount represents the annual impact of the Department’s change in regulatory policy in D.T.E. 97-112.⁸ In the Merger Order at 55, the Department stated that, for Colonial, “a change in our LBR policy that had cost consequences would be encompassed under our definition of exogenous costs.” The Department in that case also established for Colonial a monetary threshold of \$250,000. Id. at 56. The record in this case shows that the cost impact of the change in regulatory policy is \$1,034,093, which exceeds the threshold established by the Department in the merger case. Therefore, the Department finds that the Company has met the first two of the Department’s conditions for the proposed recovery of exogenous costs. That is, the cost change is of a type that is external to the Company, and the magnitude of the cost change exceeds the established monetary threshold.

The question remains as to whether the Company’s earnings were such that the Company would not warrant recovery of the \$1,034,093 in LBR. The record shows that the Company’s 2001 return on equity (“ROE”) was 3.21 percent (Exh. KSE-3). Colonial’s ROE

⁸ This amount is the difference between the total LBR amount of \$1,322,915 and the LBR amount of \$288,823 calculated based on the Department’s rolling-period method (Exh. D.T.E. 1-14).

for year 2000 was 2.78 percent (id.). These returns are significantly lower than the ROE allowed by the Department for LDCs in the most recently litigated rate cases. See Berkshire Gas Company, D.T.E. 01-56, at 119 (2002); Fitchburg Gas and Electric Light Company, D.T.E. 98-51, at 127 (1998). Further, the Company has already recovered, subject to refund, the LBR amount in question. Consequently, a rejection of the Company's proposal would further reduce Colonial's earned ROE. The Department concludes that the level of Colonial's earnings for 2000-2001 warrants approval of the Company's petition for recovery of the \$1,034,093 in LBR. Therefore, the Department finds that the Colonial has met the third condition of the Department's three-pronged test for proposed recovery of exogenous costs. Accordingly, the Department will allow for the recovery of the LBR as an exogenous cost in this case.

V. ORDER

Accordingly, after due notice, hearing and consideration, it is

ORDERED: That the savings estimates for Colonial's DSM measure installations for the period May 2000 through April 2001 are hereby approved; and it is

FURTHER ORDERED: That the Company shall recover total lost base revenues of \$1,322,915 associated with its demand-side management programs for the period May 2000 through April 2001.

By Order of the Department,

Paul B. Vasington, Chairman

James Connelly, Commissioner

W. Robert Keating, Commissioner

Eugene J. Sullivan, Jr., Commissioner

Deirdre K. Manning, Commissioner

Appeal as to matters of law from any final decision, order or ruling of the Commission may be taken to the Supreme Judicial Court by an aggrieved party in interest by the filing of a written petition praying that the Order of the Commission be modified or set aside in whole or in part.

Such petition for appeal shall be filed with the Secretary of the Commission within twenty days after the date of service of the decision, order or ruling of the Commission, or within such further time as the Commission may allow upon request filed prior to the expiration of twenty days after the date of service of said decision, order or ruling. Within ten days after such petition has been filed, the appealing party shall enter the appeal in the Supreme Judicial Court sitting in Suffolk County by filing a copy thereof with the Clerk of said Court. (Sec. 5, Chapter 25, G.L. Ter. Ed., as most recently amended by Chapter 485 of the Acts of 1971).